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Branch Banking in Ohio Under Senate Bill 256

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BRANCH BANKING IN AMERICA has primarily been a development of the twentieth century. With the advent of industrialized urban areas throughout the nation came the growth of branch banking. At the turn of the century, only five national and 91 state banks were operating a total of 119 branches. By the end of 1923, however, there were 91 national and 580 state banks with a total of 2,054 branches. The McFadden Act was enacted in 1927 in an effort to promote "competitive equality" between state and national banks by permitting national banks to have branches in those cities where state law permits state banks to have branches.

The Depression brought about modern day controversy over branch banking. Restrictive branch banking laws were primarily enacted in response to a fear of over-banking which was prevalent during the years following the Depression. Bank failure was a common occurrence during the Depression years. In the dozen years following 1921, a billion dollars of losses to bank depositors made the size and structure of the individual units in the American banking system of tremendous significance. The relatively high rate of failure among the smaller banks led some to believe that unit banking in America had seen its final days, and that such failures were due to

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3. 68 Cong. Rec. 5815 (1927).


5. This overbanking had its origin in the 1920's. During that time, there was a shift from demand to time deposits at commercial banks. This shift, accompanied by relatively liberal reserve requirements, permitted the banks to participate heavily in the underwriting of both real estate and security market speculation. The Federal Reserve Board failed to isolate speculation loans from production loans, thus resulting in a pattern of very high rates on loans in the security markets which, in turn, acted almost as a vacuum, sucking funds in from all other uses. With the crash of the stock market, the Federal Reserve Board quickly reversed its position, reducing its rates and increasing open market purchases in an attempt to bolster the financial sectors of the quickly contracting economy. With the withdrawal of England from the gold standard in 1931, the Federal Reserve system was faced with a massive gold outflow. The rush to restore liquidity led to a wave of selling on the stock market which led to a depression that was relatively more severe than that in 1929. The liquidity crisis continued until the spring of 1933; it ended only after it had brought on the failure of more than 4,000 banks in that year, widespread business bankruptcy, and the virtual closing of the Federal Reserve banks and all commercial banks during the panic that struck early in that year.


7. Unit banking is a system of banking which disallows branch banking but may allow facilities, called auxiliary teller's windows, which can accept deposits and exchange currency, but cannot make loans or investments. See Gup, A Review of State Laws on Branch Banking, 88 Banking L.J. 675 (1971).
the existence of small, undercapitalized rural banks which should be sup-
planted by branches of larger and stronger banks.  

On the other hand, those maintaining the view of the small and inde-
pendent bankers felt that the centralization of banking would pose a threat
to "the spirit of American independence." The failures of several large bank
holding companies also brought attention to problems peculiar to centralized
banking.

Ohio, like many other states, enacted legislation governing the forma-
tion of branch banks within the state. This branching law was originally
set forth in General Code Section 710-73:

No branch bank shall be established until the consent and the approval
of the superintendent of banks has been first obtained, and no bank
shall establish a branch bank in any place other than that designated in
its articles of incorporation, except in a city or village contiguous thereto.

Presumably intending to enable more viable banks to proliferate, the
Ohio General Assembly, in 1933, repealed the original branching law and
enacted legislation allowing limited branching. This legislation remained
in effect for forty-five years. It was not until April 27, 1978, that a major
change in Ohio's branching law was passed, with the enactment of Amended
Substitute Senate Bill 256.

I. THE BRANCH BANK IN OHIO

The definition of "branch" is found in Section 1101.01 of the Ohio
Revised Code. There it states that a "branch" is "an office or other place at
which a bank receives money or its equivalent from the public for deposit
and conducts a general banking business, but does not include a bank's
principal place of business."

Certain facilities, by law, are not considered to be branches, although

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8 Hearings Before a Subcomm. of the Senate Comm. on Banking and Currency Pursuant to S.
of Currency).
9 74 CONG. REC. 1129, 1130 (1930).
10 OHIO GEN. CODE § 710-73 (Baldwin 1921).
11 OHIO GEN. CODE § 710-73 (Baldwin 1933); OHIO REV. CODE ANN. § 1111.03 (Page 1953).
Limited branch banking refers to branching that is restricted to a relatively small geographic
area. The 1933 Act allowed countywide branching in Ohio.
12 Am. Sub. Senate Bill 256 was introduced in the Senate on May 3, 1977, and passed in
the Senate on October 20, 1977. The bill passed the House of Representatives on April
27, 1978. It was presented to Governor James A. Rhodes on May 19, 1978. It became
effective without the Governor's signature as it was not signed or returned to the Senate
within ten days after being so presented.
they can be operated by a bank. The first type of facility is any place, such as a school, hospital, or a commercial, retail, or manufacturing establishment, at which a person other than a bank conducts business and at which the bank itself receives items for subsequent deposit from the establishment or its employees, or from students or other persons, but not from the general public. The second type includes any location where items are received by mail, armored car service, or other delivery service, but again, for subsequent deposit.

The third type of facility is one located within a radius of one hundred yards (or, with the approval of the Superintendent of Banks, five hundred yards) of the principal place of business of a bank, or a branch of such bank, which the superintendent finds is an extension of the services of such office or branch. The last exception is that of a facility located on a military installation where a bank accepts deposits and cashes checks.

The Revised Code provides for two other types of offices; the intermittent branch, which serves primarily as a temporary office, subject to various limitations concerning operations; and the seasonal agency, which may be established for service in resort communities.

The laws governing the formation and operation of these branch banks are embodied mainly in Sections 1111.02 and 1111.03 of the Ohio Revised Code. There are three basic provisions in these laws: (1) geographic considerations, (2) procedural requirements, and (3) statutory criteria used by the Superintendent of Banks in the evaluation of branch applications. In order to establish a branch, each of these areas must be dealt with by the applicant bank so as to merit the consent of the superintendent. A brief comparison of these three elements under the old and the new law demonstrates the evolution to the present state of the law.

II. BANK BRANCHING IN OHIO BEFORE 1979

A. Geographic Considerations

Prior to the enactment of Senate Bill 256, the branching laws prohibited any bank from establishing a branch in any place other than that designated in its articles of incorporation as its principal place of business. Exceptions included a municipal corporation contiguous to such designated

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14 Id. § 1101.01(E)(1).
15 Id. § 1101.01(E)(2). In First Nat'l Bank v. Dickinson, 396 U.S. 122 (1969), the United States Supreme Court recognized armored car service as a proper form of branch banking.
17 Id. § 1101.01(E)(4).
19 Id. § 1111.05.
20 Id. § 1111.03(A).
place, or other parts of the county in which the principal place of business of the bank was located. A bank was also permitted to maintain a branch outside the United States subject to approval and satisfaction of the superintendent.

Another exception to the countywide limitation was recognized when the municipality set forth in the bank's articles of incorporation as its principal place of business was located in more than one county. In such instances, the bank was allowed to branch into each of the counties in which its principal place of business was located.

B. Procedural Requirements

Upon receipt of a branching application, the prior law required the Superintendent of Banks to give written notice of its filing to every other bank in the county where the proposed branch was to be located and to those within fifteen miles of the proposed branch. At the same time, or before forwarding such application, the applicant bank was required to publish notice for a period of two weeks following the filing of the application in a newspaper of general circulation in the county where the proposed branch was to be located.

The superintendent was required to "conduct such investigation as he deem[ed] necessary," and he had full discretion as to whether hearings should be held before the Division of Banks or the banking board. Action on the branch application by the superintendent was to be completed within ninety days of its filing, unless an extension of time was granted by the applicant bank.

21 The Attorney General has dealt with the meaning of the word "contiguous" on three occasions. The Attorney General ruled that: (1) "A state bank may establish branches in those cities and villages which touch or abut upon the place designated in its articles of incorporation for the transaction of its business." 1920 Op. Att'y Gen. 1066 (1920); (2) "Where two banks, located in two cities or villages in the same county, the boundary lines of which do not touch, consolidate, or one transfers its assets to the other, general banking business cannot be conducted at both the original locations of such banks." 1920 Op. Att'y Gen. 1189 (1920); and (3) "When a bank has a legally established branch in a village contiguous to the village in which its principal place of business is located, such bank may file with the Secretary of State its amended articles of incorporation changing its principal place of business to that of its branch bank, which articles may be recorded by the Secretary of State upon the issuance to him by the Superintendent of Banks of a certificate approving such amendment." 1931 Op. Att'y Gen. 826 (1931).

22 1id. § 1111.03(A) (Page Supp. 1968).

23 Id. § 1111.03(B).

24 There are at least 32 Ohio municipalities which cross county lines.


26 1id. § 1111.02(A) (Page Supp. 1977).

27 Id. § 1111.02(B).

28 Id.

29 Id.

30 Id. § 1111.02(C).
During the processing of the application, the applicant bank was required to submit to the superintendent proof of publication of its application notice and evidence that suitable property was available upon which to establish the branch. In those cases in which the superintendent elected to submit the application to the banking board for hearing, he was required to notify the applicant bank of the time and place at which the board would convene.

C. Statutory Criteria Used In Application Evaluation

Under the prior law, the superintendent, in considering an application for a branch bank, was required to ascertain: whether the convenience and needs of the public would be served by the proposed branch; whether the population and economic characteristics of the area primarily to be served by the branch afforded reasonable promise of adequate support for the proposed branch; and whether the proposed branch met such other reasonable criteria as the superintendent might require.

Those "other reasonable criteria" were set forth in the regulations. Under the regulations, the superintendent considered: the adequacy of the capital structure of the applicant bank; the general character of the management of the applicant bank; the financial history and condition of the applicant bank; and any and all other pertinent factors relating to the establishing of such branch.

Finally, the proposed branch was required to meet the minimum capital, surplus, and undivided profits requirements specified in the Revised Code. Such amounts were not permitted to aggregate less than $100,000.

Upon approval of its application, the applicant bank was required to establish its branch within one year from the date of the superintendent's
approval, unless good cause could be shown by the applicant bank for requesting an extension. 44

III. RECOGNITION OF THE NEED FOR NEW LEGISLATION

The branching laws set forth above were in effect for more than thirty-five years before they were severely criticized. With the 1970's came an increased call for banking reform. On November 15, 1971, Governor John J. Gilligan appointed twelve persons to the Supplemental Advisory Board of the Division of Banks. The Governor instructed the Board, which became known as the Ohio Bank Study Commission, to "advise and consult with the Division of Banks of the Department of Commerce on matters affecting banking regulations, especially the formulation of legislative proposals and complementary legislation." 45

In making its recommendations, the primary objective of the Commission was:

to allow and encourage the banking system to be more responsive and more competitive. In as many ways as possible, the system should be enabled to respond to expanding opportunities for serving the needs of the public. The regulatory authority should be reluctant to stand in the way of vigorous innovation by banks acting under the influence of strong competitive motives. 46

A major area in which the Commission made extensive recommendations was that of branching. The Commission considered the system of bank branching then in effect to be an archaic concept in light of the modern developments in communications, transportation, shifts in population and economic centers, and expansion of banking services. The Commission concluded that the present constraints of countywide branching were no longer appropriate. 47

The Commission noted that logical expansion of banking services beyond political boundaries was a natural development of the growth of the economy and markets, and such expansion had been limited primarily to the holding company method, which provided, in effect, statewide branching. 48 The report also noted the anomalous situation created by the law in that banks located in municipalities situated in two or more counties could branch into those counties while all other banks were restricted to a single county. 49

46 Id. at 5.
47 Id. at 13.
48 Id.
49 Id. See text accompanying notes 24-25 supra.
In light of these considerations, the Commission recommended that the Ohio General Assembly, at an early date consider contiguous county branching or market area branching, and statewide branching de novo or by acquisition or merger. The Commission further proposes that the General Assembly take into consideration the need for a transitional period to meet both the administrative problems of regulatory agencies and the capability of the banking system to adjust to whatever change may be authorized. 50

Between the time the Commission issued its report and the introduction of Senate Bill 256, it became obvious that the banking industry in Ohio was in the midst of major change. It became equally obvious that branch banking had become the dominant form of banking in Ohio. In 1975, 340, or 69%, of the 496 banks in Ohio were operating branches. Of the $30,579,000,000 on deposit in Ohio banks in 1975, 95%, or $29,069,000,000, were controlled by banks with branch offices. 51

The question of statewide branching was finally brought to the forefront. House Bill 930 was introduced in the Ohio General Assembly in 1976, which called for statewide branching. The bill was passed in the House, but died in the Senate.

Finally in May, 1977, came the introduction of Senate Bill 256 by Senator Harry Meshel (D) of the 33rd Senatorial District. 52 The passage of the bill, with its several amendments and substitutions, was the culmination of the recommendations made six years earlier by the Ohio Bank Study Commission.

IV. BANK BRANCHING IN OHIO AFTER 1978

A. Geographic Considerations

The establishment of a branch through consolidations, purchases, acquisitions, or other transfers of assets or liabilities, including corporate reorganization, is allowed anywhere in the state immediately after the effective date of January 1, 1979. 53 A bank acquiring another bank in such a manner would be permitted, with the permission of the superintendent, to maintain

50 Id. THE REPORT OF THE PRESIDENT'S COMMISSION ON FINANCIAL STRUCTURE AND REGULATION (THE HUNT COMMISSION REPORT) (1973) suggested that "by state laws, the power of commercial banks to branch, both de novo and by merger, be extended to a statewide basis, and that all statutory restrictions on branch or home office locations based on geographic or population factors or in proximity to other banks or branches thereof be eliminated." HUNT COMMISSION REPORT at 61-62.
51 David E. Sisk, The Question of Statewide Branching in Ohio, ECONOMIC COMMENTARY, October 4, 1976 at 1.
all existing or authorized branches of the constituent bank, establish branches in the county in which the constituent bank maintained its principal place of business, and establish branches in any county contiguous to the county in which the constituent bank maintained its principal place of business. Other branching is being phased into statewide status by being restricted to contiguous county branching after the effective date of the new law and will subsequently be made statewide after January 1, 1989.

Thus, as a rule, de novo branching can now be implemented with the consent of the superintendent, provided that from January 1, 1979, to January 1, 1989, the branch is located in the place designated as the bank's principal place of business by its articles of incorporation, in municipal corporations contiguous thereto, in the rest of the county in which the bank's principal place of business is located, or in any county contiguous thereto. After January 1, 1989, all branching will be allowed statewide.

As of the effective date of the Act, a bank may establish branches which primarily transfer funds by electronic means in the county in which the bank maintains its principal place of business, or in any other county in which the bank maintains a branch that is staffed by a full-time loan officer and which offers loans of the same type and in the same amounts as those offered at the bank's principal place of business or branches in the county in which the bank's principal place of business is located.

B. Procedural Requirements

The procedure for processing a branch application now is essentially the same as under the prior law, except that notice by the applicant must be published in the county where the bank maintains its principal place of business as well as in the county where the branch is to be located. The superintendent must hold a public hearing if a written objection to his findings

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54 Id. § 1111.03(A)(2)(a).
55 Id. § 1111.03(A)(2)(b).
56 Id.
57 Id. § 1111.03(A). "Contiguous" is defined as including "counties that abut or come in contact at any point either on land or within a body of water." Id. § 1111.03(A)(4). See also 1920 Op. Att'y Gen. 1066 (1920).
59 Id. § 1111.03(A)(1).
60 Such means include automated teller machines (ATM's) and customer bank communications terminals (CBCT's). Ohio follows the rule set down in Independent Bankers Ass'n of America v. Smith, 534 F.2d 921 (D.C. Cir. 1976). See also "New Directions in Ohio: In-Store Bank Branches, THE OHIO BANKER, May, 1976 at 10.
62 Id. § 1111.03(A)(5)(b).
63 Id. § 1111.02(B).
is issued within thirty days after publication of the bank's application notice.\textsuperscript{64} Prior to such hearing, the superintendent must issue his preliminary findings as to whether the applicant bank has met the various criteria required by law,\textsuperscript{65} as well as a summary of the information submitted to the superintendent by the applicant bank.\textsuperscript{66} Also, the application fee for a branch bank was increased from five hundred dollars to one thousand dollars.\textsuperscript{67}

C. Statutory Criteria Used In Application Evaluation

Aside from the geographic restrictions, the most significant changes in the branching laws brought by Senate Bill 256 were in the statutory criteria to be met by the applicant bank. Two express prohibitions on the approval of a branch by the superintendent have been incorporated into the law. First, the superintendent may not approve a branch if he “determines that such approval would cause the applicant bank to control aggregate total deposits of banks in the state exceeding twenty percent of the total deposits held by all banks located in [the] state.”\textsuperscript{68} The second restriction requires that no application for relocation of a principal place of business shall be approved “if the superintendent determines that the sole purpose of the relocation is to establish and maintain a branch.”\textsuperscript{69}

The applicant bank must still demonstrate that the convenience and needs of the public will be served by the proposed branch,\textsuperscript{70} and that the population and economic characteristics of the area primarily to be served by the branch afford reasonable promise of adequate support for the proposed branch.\textsuperscript{71} The “other reasonable criteria” set forth in the regulations have been retained as well.\textsuperscript{72} However, the new law adds some additional criteria to be considered by the superintendent as well.

First, the superintendent must determine whether the applicant's lending record meets the credit needs of the entire community, including low and moderate income neighborhoods, and is consistent with the safe and sound operation of the applicant and the Community Reinvestment Act of 1977,\textsuperscript{73} as well as the rules and regulations\textsuperscript{74} promulgated under that Act.\textsuperscript{75} Second,
the superintendent must determine that the applicant has neither denied mortgage loans nor varied the terms on the basis of neighborhood location or age of the security for such loan. If the applicant has done so, the denial must have been justified and the variance necessary to avoid an unsound banking practice.76

Finally, the superintendent must determine whether the applicant "intends that the primary purpose for the branch is to meet the credit needs of the local community where the branch is to be established, consistent with sound banking principles."77

In the event that the superintendent determines that any of the criteria set forth above are not satisfied, he is then required to withhold his approval and notify the applicant of his decision and the reasons upon which it is based. If the criteria not met are those set forth in Sections 1111.03(C)(3) or 1111.03(C)(4), the applicant is then required to submit to the superintendent a written affirmative action lending program, which shall be made part of the public record.78 The superintendent must determine within thirty days whether such program is acceptable and either approve or deny the application.79

Once such a program is approved, the superintendent may require the bank to report periodically as to what steps have been taken by said bank to implement its affirmative action program.80 Upon written complaint by any person, or upon his own initiative, the superintendent may hold a hearing to determine compliance. No more than one such hearing may be held every two years.81 If the superintendent determines noncompliance, he must order compliance within a period of time determined by him.82 The laws concerning minimum capital, surplus, and undivided profits requirements remain unchanged.

76 Id. § 1111.03(C)(4).
77 Id. § 1111.03(C)(5).
78 An affirmative action lending program is defined as "a program to remedy any deficiency of an application in meeting the credit needs of an entire community. If the deficiency is related to construction, rehabilitation, or maintenance of housing, the program shall contain, but not be limited to, one or more of the following: (1) advertising the availability of such loans; (2) providing a credit denial review program to applicants, providing facilities, services, and resources to establish programs for neighborhood preservation and reimbursements." OHIO REV. CODE ANN. § 1111.03(E) (Page Supp. 1978). Also required in the program is a written statement of lending standards which implement the criteria set forth at id. §§ 1111.03(C)(3), (4).
80 Id. § 1111.03(F)(1)(b).
81 Id. § 1111.03(F)(1)(a).
82 Id. § 1111.03(F)(2).
V. ADMINISTRATION PROCEDURE AND THE NEW BRANCHING LAW

It is significant that the new law embodies a more realistic and effective approach to branching which will enable Ohio banks to continue to serve and to respond to their ever-changing customer markets. The law provides for such service and responsibility to be carried out under the continuing supervision of the Superintendent of Banks but without imposing upon him complex administrative proceedings. For example, the requirement for hearings by the superintendent is highly discretionary, to be decided on a case-by-case basis. This approach is wholly consistent with the current law in that the Superintendent of Banks is not subject to the Administrative Procedure Act with regard to the approval or denial of branch applications. The present state of the law on this issue is set forth in *Home Savings and Loan Association v. Boesch*, in which the Ohio Supreme Court ruled that approval of a building and loan association's application for a branch bank facility is not a licensing function under the provisions of the Administrative Procedure Act.

While this case dealt with branch approval given by the Superintendent of Building and Loan Associations, the court recognized that the statutes under which the superintendent in *Home Savings* granted such an approval are similar to the current branch banking statutes and, therefore, relied upon their meaning in reaching its decision. Thus, one is strongly persuaded that the same reasoning and syllabus would be applicable to a determination by the Superintendent of Banks when approving or denying a branch bank application. Further, the superintendent has acted consistently with the guidelines set down in *Home Savings* since it was decided.

Removing a branch application approval from the scope of the Administration Procedure Act has a highly practical advantage. If the superintendent's determinations regarding branch applications were governed by the provisions of the Administrative Procedure Act, the Act would provide fertile ground for any opponent of an approved branch application to perfunctorily seek a court order suspending the superintendent's approval without any showing of irreparable damages as is otherwise required under Rule 65 of the Ohio Rules of Civil Procedure. Further, it is foreseeable that

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86 41 Ohio St. 2d 115, 119, 322 N.E.2d 878, 880 (1975).
87 *Id.*
such an opponent could, by way of a Section 119.1289 suspension, easily frustrate and delay for several years the implementation of the superintendent's branch approval causing great economic loss to the bank, both in the delay of the branch opening and in costly expenditures for needless litigation.

Finally, it is important to point out that anyone opposing the superintendent's branch determination is not without recourse. Presumably, traditional avenues of reviewing a public official's action through injunctive relief or declaratory judgment continue to be available.

VI. THE CONTROVERSY OVER STATEWIDE BRANCHING

The antiquated and restrictive nature of branching laws, both on the state and federal level, has been constantly under fire during the past few years. On the national level, Senator Thomas J. McIntyre (D-N.H.), chairman of the Senate Subcommittee on Financial Institutions, has criticized the McFadden Act,90 stating:

It is ludicrous that in 1976 the authority of banks to branch in many jurisdictions is based upon laws and practices — not designed to promote competition — but designed instead to insure that existing institutions however non-competitive, will not be adversely affected! . . . The plain fact is that the laws adopted by Congress in 1927 and 1933 have made it possible for banks to carve up their markets in such a way as to insulate themselves from competition and thus from serving the public to a maximum degree.91

On the state level, proponents of statewide banking in Ohio expressed essentially the same sentiments prior to the passage of Senate Bill 256. The factions in the banking industry in Ohio were clearly split. On one side, encouraging the passage of the bill, was a loosely knit group of bank holding company organizations, as well as liberal banking groups such as the Ohio Association for Modern Banking. Opposed to the bill was a more tightly knit organization known as the Community Bankers Association of Ohio, which was primarily composed of small independent banks throughout Ohio.92 The largest of the bank organizations, the Ohio Banks Association,

89 OHIO REV. CODE ANN. § 119.12 (Page 1977) provides for appeal from an agency order by one adversely affected by such order. Upon a showing that an unusual hardship to the appellant will result from execution of the agency's order, pending determination of the appeal, the court may grant a suspension and fix its terms.
91 Letter from William P. Lewis, Counsel for the Ohio Ass'n for Modern Banking, to Senator Harry Meshel, (March 31, 1976). See also 50 Years of McFadden: Impasse for Banking Growth, BANK STOCK QUARTERLY, December, 1976 at 15.
92 Interview with Jerry Woessner, Deputy Manager of the Ohio Bankers Ass'n, Columbus, Ohio, (September 21, 1978).
maintained a neutral position on the bill, offering no input regarding the legislation.98

The independent banks were clearly against the bill. On January 6, 1977, the Community Bankers Association of Ohio released the results of a poll taken among independent banks in Ohio. Almost forty-five percent of the commercial banks in Ohio responded to the poll. Of the 68 responding banks which were members of the Community Bankers Association of Ohio, 64 were in favor of no change in the state branching laws (that is, they were in favor of countywide branching); 2.5 were in favor of contiguous county branching; 1.5 were in favor of regional contiguous branching; and none were in favor of statewide branching. Among the 91 respondents which were not members of the Association, 75 preferred countywide branching; eleven were in favor of contiguous county branching; one was in favor of regional contiguous branching; and only four were in favor of statewide branching.94

Likewise, small, independent businesses were opposed to passage of the bill. In a poll taken in 1977 by the National Federation of Independent Business, sixty-four per cent of owners of small businesses polled in Ohio said that they were opposed to statewide branching; twenty-three per cent were in favor of the bill, and thirteen per cent were undecided. Of the same group of businessmen, sixty-six per cent preferred to do business with an independent bank; seventeen per cent preferred a major state bank or a branch thereof, and seventeen per cent had no opinion.95 Thus, it is clear that the attitude among small businesses concerning statewide branching is a function of the preference among such small businesses of using independent banks to meet their financial needs.

Opponents to statewide branching generally feel that it will result in the small independent banks being squeezed out by the larger banks. The point is often made that in statewide branching states there is a more concentrated amount of deposits in the few largest banks, thus causing the undercapitalization of the smaller banks. In California, for example, a statewide branching state, the nine largest banks in the state control more than 86% of the total deposits and they operate nearly 80% of the branch facilities.96 Opponents of the bill also cited as examples the various unit banking

98 Id.
94 Letter to all independent banks from A. Richard Smith, Executive Director of the Community Bankers Ass'n of Ohio, (June 6, 1977).
95 Letter to A.C. Liest, President of the Apple Creek Banking Co., from R. Hal Nichols, Superintendent of Banks, (June 23, 1977).
96 Testimony of Raymond D. Campbell, President and Chief Executive Officer of the Oberlin Savings Bank Co. before the Ohio Senate Committee on Elections, Financial Institutions and Insurance, (June 8, 1977) at 4.
states. In a comparison of Ohio with Texas, a unit banking state, the percentage of total deposits in the five largest commercial banks by standard metropolitan statistical area as of June 30, 1976, showed the five largest banks in Cleveland, Ohio, held 85.9% of total deposits while the five largest in Houston, Texas, held only 50.9%. In the one year period from June 30, 1975, to June 30, 1976, total bank deposits in Texas increased from $43,374,246,000 to $48,094,190,000, an increase of 10.9%. In Ohio, during the same period, total deposits increased from $29,521,831,000 to $30,842,795,000, an increase of only 4.7%. Thus, it appeared to the independent banks that more growth was possible under stringent branching laws.

The proponents of the bill, however, asserted that the fears of the independent banks were not well grounded. Rather, they held that more liberal branching laws would allow management greater flexibility to respond to market forces in providing the public with convenient banking services and that it would result in increased competition.

A primary concern was the ability of commercial banks to compete with other financial institutions. With the growth of "checking" powers among savings and loans and thrift institutions and the proliferation of savings and loan remote service units (RSU's), many saw restrictive branching laws as a hindrance upon the commercial bank's ability to compete:

Branching restrictions will not be able to protect the markets of individual institutions even if that were a desirable objective. They will only inhibit the development of full competitive vigor of Ohio financial institutions to their long run detriment in competing with others and to the public's disadvantage. We are not faced with an alternative of preserving local markets for local institutions by keeping out outsiders; rather, we are faced with the question of whether or not to give Ohio commercial banks the chance to compete equitably with other institutions in providing convenient financial services to the public. A shift from countywide to statewide branching will facilitate that competition.

Four particular "items of conjecture" expressed by opponents to the bill as the evils of liberalized branching can easily be shown to be myth rather than fact.

The first such item is the belief that the larger banks will "gobble up" the smaller banks. Most of the bill's opponents feel that this will take place

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97 Testimony of Raymond D. Campbell, President and Chief Executive Officer of Oberlin Savings Bank Co. before the House Committee on Economic Affairs and Federal Relations, (Feb. 28, 1978) at 1.


99 Id. at 2-3.
through mergers. However, a close look at the new law reveals that such predatory take-overs will not occur. First, the applicant bank must demonstrate that the convenience and needs of the community will be better served and that no individual bank nor competition in general will suffer an unjust detriment before a merger can occur. Second, the new law places a ceiling on growth by merger or acquisition.

Statistics show that small banks can prosper in statewide branching states as well as in restrictive branching states. In 1975, California had 88 more banks in existence than in 1960. Sixty-seven percent of California banks were under $50,000,000 in deposits and forty-eight percent were under $25,000,000. Ohio, operating under restrictive branching laws, had 85 fewer banks in 1975 than in 1960. Eighty percent of Ohio's banks were under $50,000,000 and sixty-one per cent were under $25,000,000. Both states have a substantial proportion of small banks, but Ohio has about twenty-five per cent more than California. This somewhat larger proportion of small banks in Ohio, however, is not surprising since growth into larger, more viable institutions comes largely from bank expansion. In any case, these figures demonstrate that small banks can prosper and new banks can be organized under statewide branching.

Another fear of opponents is that branch banks will suddenly appear on every street corner. This also can be shown to be unlikely under the new law. First of all, the economic criteria to be met by the applicant bank preserves the convenience and needs of the public and assures that the area to be served can adequately support the proposed branch. In addition, many of the small communities in which opponents to statewide branching are located are not suitable areas into which a commercial bank would branch. Finally, all the commercial banks in the state must work within financial constraints. Having limited funds with which to establish branches, a commercial bank will by necessity branch only into those areas where it hopes to get a return; "[m]otivated by a desire to maximize profits, a banker will expand operations so long as the revenue derived from additional trans-
actions covers the cost of making them."\(^{109}\) Thus, even the large commercial banks will be forced to make rational business judgments in terms of where to branch and how many branches should be established.\(^{110}\)

The third item is the belief that large branch banks will siphon funds from rural areas into the large cities. This argument assumes that banks, which are organized to generate a reasonable return on equity for their shareholders, can make a greater profit in the cities than in the less urbanized areas. But,

\[\text{[T]his simply is not true. First, banks in the metropolitan areas of Ohio generally have the largest available pool of loanable funds in absolute dollars of any segment of the banking industry. Prudent management and regulatory agency supervision deter excessive extensions of credit beyond the normal trading area for the individual banks. These funds, therefore, are invested in other ways, usually at a lower yield than prevailing loan rates. Second, average net loan portfolio yields of metropolitan banks, who experience extensive credit requests from prime or near prime rate borrowers, tend to be lower than portfolio yields of banks in residential communities with relatively higher consumer loan demand.}\]

\[\text{It is very doubtful that big city banks with excess funds to loan and with relatively lower portfolio yields would want to siphon more funds into the cities.}\(^{111}\)

Finally, there is the belief that small banks do a better job of serving their customers. But as one commentator has said, "[q]uality of service is a function of management, not of size."\(^{112}\) Perhaps the best measure of such quality is the loan to deposit ratio maintained by the various banks. Generally, a loan to deposit ratio of 80% is the maximum, and 70% is a more practical ceiling.\(^{113}\)

As of June 30, 1976, all of the banks in Ohio had an average loan to deposit ratio of 64.08%.\(^{114}\) A breakdown by counties shows that three counties had total bank average loan to deposit ratios of 70-79%; 51 had averages of 60-69%; 28 had averages of 50-59%; five had averages of 40-49%; and one had an average of 30-39%.\(^{115}\)

Fifty-four of Ohio's 88 counties are at or above the state average. This


\(^{110}\) Testimony of Dr. Douglas V. Austin, supra note 108 at 3.

\(^{111}\) Testimony of John R. Hanschmidt, supra note 102 at 3.

\(^{112}\) Id. at 4.

\(^{113}\) Id.

\(^{114}\) Id.

\(^{115}\) Id. at 5.
means that these counties are "capital starved" since the loan demand exceeds the ability of banks to fulfill that demand from local deposits. Under the new law, banks with available funds will be able to branch into these counties to help alleviate the credit shortage.

Conversely, thirty-four of Ohio's eighty-eight counties are below the state average loan to deposit ratio. There are two possible reasons for the low ratio of these counties. One might be a prevalence of conservative financial institutions which are unwilling to serve the loan needs of the community. The other might be soft loan demand which results in excess funds available for loans. Given the probability that the conservative reason is more the exception than the rule, it may be safe to assume that soft loan demand resulting in available funds causes the low ratio in these counties. Whereas the prior law restricted these banks from branching into capital starved counties, the new law allows such branching and therefore works to strengthen the banking industry as well as the economy.

These statistics show that some areas of the state have excess capital, while others are capital deficient. The new law, by removing the artificial county line barriers to bank branching, allows the rendering of bank services in a competitive open market environment.

In addition to alleviating the problems foreseen by the independent banks, the new law also alleviates two anomalous situations existing within the banking industry itself.

The first such anomaly was the situation in which a bank's principal place of business was located in more than one county. Such banks were previously at an advantage in that they could branch throughout all counties in which such principal places of business were located. The new law places all Ohio banks on equal terms with regard to the potential for expansion of services through branching.

The second anomaly is found in the system of bank holding companies operating in Ohio. Bank holding companies have been permitted to operate statewide since 1929 in the State of Ohio. In fact, bank holding companies are operating de facto branching systems throughout the state. In effect, the state legislature has permitted commercial bank branching statewide through the vehicle of the bank holding company, but has not afforded the same opportunity to independent banks which do not desire to form holding companies. As a result, those commercial banks which desire to be competitive with bank holding companies within portions of the state or throughout the state are at a serious competitive disadvantage. The new legislation permits
a theoretical competitive par to be established between those banks that wish to operate on a regional basis, those which desire to operate statewide through a commercial banking format, and those bank holding companies which wish to operate statewide through affiliate banks and expanded branching. One result of the new legislation has been described as follows:

As proposed, January 1, 1989, would trigger statewide branching for all banks regardless of legal structure, and it would not be surprising . . . that some of today's current bank holding companies might convert to branch banking systems prior to 1989 and operate statewide as a de jure statewide branching system.\(^{118}\)

The holding companies are now able to do so under the new law on bank reorganizations.\(^ {118}\) According to the new provisions, each holding company may, through a corporate reorganization, become a bank, retain its affiliates and their branches, and be able to branch into counties contiguous to that one in which each affiliate has its principal place of business.\(^ {120}\) Because reorganization may take place anytime after the effective date of the Act, January 1, 1979, the holding companies are given an advantage over the smaller banks in terms of the geographic constraints and seemingly extending the anomaly for another ten years. However, as of January 1, 1989, parity will finally be reached between all banks, large and small, in terms of their capacity to branch anywhere in the state, thus alleviating this long-lived inequity.\(^ {121}\)

Thus, it is clear that liberal bank branching statutes are more advantageous than detrimental to the banking industry as a whole. In addition, the comparative merits of liberalized branching to the status quo is a moot issue. Perhaps more important are the implications of more liberalized branching in the dual banking system.

\(^{118}\) Testimony of Dr. Douglas V. Austin, Former Chairman of the Ohio Bank Study Comm'n, before the House Committee on Economic Affairs and Federal Relations, (February 15, 1978) at 4.


\(^{120}\) See text accompanying notes 54-56 supra.

\(^{121}\) An interesting sidelight in terms of bank holding companies and their capacity to branch statewide is seen in the names of the various holding companies. The prior branching laws restricted the branching of "banks" to the county in which each bank had its principal place of business. Of the 32 bank holding companies in Ohio, none have the word "bank" in their names. In fact, 13 of the names include the word "banc" instead, e.g., BancOhio Corporation, Huntington Bancshares, Inc., First Banc Group of Ohio, Inc., etc. The reason for this, presumably, was that a "bank" was not able to branch outside its own county, while holding companies could branch de facto anywhere in the state; hence "bank" was left out of the names of these organizations and "banc" was used instead. Since the new law allows the holding companies to reorganize and branch as "banks," it will be interesting to see if any of these names change.
VII. PROBLEMS WITH THE FEDERAL-STATE
DICHOTOMY UNDER THE NEW BRANCHING LAW

Inherent in the dual banking system is the presence of competition between state-chartered and federally-chartered banks. Among the competitive fields in the dual banking system is that of bank branching. The branching laws for national banks are presumably maintained to promote "competitive equality" among the state and federal banks:

A national banking association may, with the approval of the Comptroller of the Currency, establish and operate new branches: (1) Within the limits of city, town, or village in which said association is situated, if such establishment and operation are at the time expressly authorized to State banks by the law of the State in question; and (2) at any point within the state in which said association is situated, if such establishment and operation are at the time authorized to State banks by the statute law of the State in question by language specifically granting such authority affirmatively and not merely by implication or recognition, and subject to the restrictions as to location imposed by the law of the State on State banks.

Similar applications of the state law are imposed upon branches resulting from conversion of a state bank to a national bank and consolidation of a national bank. A discussion of the applicable federal law is in order.

The procedure and economic criteria encountered in applying for a federal bank branch are primarily contained in the branching regulations. The applicant bank submits an application to the Regional Administrator of National Banks. Upon notification that such application has been received, the applicant bank must publish a notice of application both in the county in which its principal place of business is located and in that where the proposed branch is to be located. A public file is compiled containing the information and data accumulated by the Regional Administrator.

The regulations require the Regional Administrator to conduct a hear-

122 See text accompanying note 3 supra.
124 Id. § 36(b)(1).
125 Id. § 36(b)(2).
126 See OHIO REV. CODE § 1121.02 (Page Supp. 1978) for the state statute governing conversions.
128 Id. § 4.5(a).
129 Id. § 5.2(b).
130 Id. § 5.3.
ing on the application upon written request pursuant to regulations concerning the date, place, and notice of the hearing, as well as the procedure of the hearing itself. Notification of the outcome of the hearing is sent to the applicant bank and all persons who make a written request. When the application is approved, a certificate is issued evidencing such approval. Such certificate may be rescinded in the event that the applicant bank fails to commence business at its branch within eighteen months from the date of approval.

When the application is disapproved, a written statement containing the reasons for such disapproval is furnished to the applicant. While applications will not be reconsidered after disapproval, a new application for the same proposed facility may be filed by submitting new or additional substantive information to the Regional Administrator.

The various information and data considered by the Regional Administrator is based upon the policy of the Office of the Comptroller of the Currency. This office encourages a banking system "capable of fulfilling local, regional, and national needs in banking services." Such capability is determined by the consideration of various factors in the evaluation of an application.

The capacity of the applicant bank to support the new facility is of great importance. In evaluating such capacity, the Regional Administrator considers the general condition of the applicant bank, the sufficiency of capital, earnings, and retention of earnings to support both the applicant's current level of operation as well as the proposed expansion, and the ability of management to supervise a sound banking operation.

Various market factors are also considered, including the current eco-

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131 Id. § 5.4.
132 Id. § 5.6.
133 Id. § 5.5.
134 Id. § 5.7.
135 Id. § 5.10.
136 Id. § 5.13.
137 Id. § 4.5.
138 Id. § 4.5(c).
139 Id. § 4.5(e).
140 Id. § 4.5(e)(2).
142 Id.
143 Id. at 9-10.
144 Id.
145 Id. at 10.
nomic condition or growth potential of the market in determining the probable
success of the branch, as well as the same conditions in the primary service
area, the specific location of the proposed facility, and the surrounding
population. The growth rate and size of banking offices and other financial
institutions in the market are considered as well. In most respects, the
state and national economic criteria for approval of a bank branch appli-
cation prior to January 1, 1979, were essentially the same.

In 1977, Congress enacted the Community Development Act of
1977. Title VIII of that Act is the Community Reinvestment Act of
1977. The Community Reinvestment Act requires the federal supervisory
agencies to assess a financial institution's record of meeting the credit needs
of its entire community, consistent with safe, sound operation, to take such
record into account in its evaluation of an application by the institution for
a deposit facility by such institution, and to report annually to Congress
actions taken by such agency to carry out its responsibilities under the Act.

In adopting the Act, Congress recognized

the vital interconnection between successful community and housing
development and local private investment activities. The effectiveness
of the community development programs, the housing assistance pro-
grams, and the mortgage assistance programs . . . depend in large part
upon the availability of private capital, particularly as made available
through local lending and financial institutions. [The Act is] designed
to encourage more coordinated efforts between private investment and
federal grants and insurance in order to increase the viability of our
urban communities.

The inclusion of the Community Reinvestment language in Senate Bill
256 was viewed favorably. However, the problem lies in the application

146 Id.
147 Id. at 11.
148 Id.
149 Id.
150 Id. at 12.
151 See text accompanying notes 34-44 supra.
154 Id. § 2903(1).
155 Id. § 2904.
156 Id.
NEWS 2884, 2995. See also U.S. DEP’T OF HUD, SUMMARY OF THE HOUSING AND COM-
MUNITY DEVELOPMENT ACT, October, 1977, at 21.
158 See text accompanying note 73 supra.
159 Testimony of R. Hal Nichols, Superintendent of Banks, before the House Committee
on Economic Affairs and Federal Relations, (March 14, 1978) at 3; Testimony of Roman
of the Act in the federal branching laws as opposed to that in state branching laws. As was discussed previously, the state branching law contains a definite sanction to the superintendent to require an applicant bank to demonstrate that its lending record meets the credit needs of the community in accord with the Act and the regulations promulgated thereunder.\textsuperscript{160} In the absence of such a demonstration, the superintendent may require an affirmative action lending program to implement such language,\textsuperscript{161} and subsequently to deny the bank’s application if such a program is not satisfactory.\textsuperscript{162} The superintendent may also hold hearings to insure compliance and issue directives to the institutions should he determine that such compliance is lacking.\textsuperscript{163}

The federal branching statute has no Community Reinvestment language. Rather, “[I]n considering an application for the establishment of a domestic branch or other facility with the ability to accept deposits . . ., the Comptroller will take into account, among other factors, the applicant’s record of performance.”\textsuperscript{164} The bank’s record of performance \textit{may} be the basis for the denial of such an application by a national bank,\textsuperscript{165} while a poor record of performance \textit{is} the basis for denial on the state level.\textsuperscript{166} No sanction actually exists in the federal statute, thus posing the problem of enforcement. The lack of such a sanction must necessarily put the state-chartered applicant bank at a disadvantage in that its application is more difficult to have approved than that of its federal counterpart.

Similar problems exist with the other statutory restrictions added to the state branching law by Senate Bill 256.

The new Act contains “anti-redlining” language which is intended to insure against denial of loans by the applicant bank on the basis of the location or age of the security for such loans.\textsuperscript{167} Originally, in the initial stages of Senate Bill 256, this anti-redlining language, along with the primary purpose clause immediately following it, were included in the text of the bill with no mention of the Community Reinvestment Act. As the bill

\begin{flushright}
J. Gerber, Executive Vice President of First Banc Group of Ohio, Inc., before the House Committee on Economic Affairs and Federal Relations, (February 15, 1978) at 2; Testimony of Dr. Douglas V. Austin, former Chairman of Ohio Bank Study Comm’n before the Economic Affairs and Federal Relations, (February 15, 1978) at 12.
\end{flushright}
made its way through the Senate and the House, a number of people called for the removal of the anti-redlining language and the inclusion of the Community Reinvestment language. In the final form both clauses are effective, thus maintaining what many thought to be a formula against redlining which would be impossible to enforce.

A number of problems exist as a result of the enactment of the anti-redlining language. First of all, a practical problem exists in the evidentiary or factual determination of redlining practices by a commercial bank. As was testified to in legislative hearings,

\[\text{[T]he regulatory authorities don't have any definition or standards. What the legislature is trying to do by simple English phrasing is to cause an imponderable problem of attempting to force banks and/or regulatory authorities to determine that banks either are or are not redlining when no one can determine in a meaningful, statistical sense what actually is redlining.}\]

Second, there exists no enabling legislation which might provide funds for the Division of Banks to implement the affirmative action lending programs.

Finally, the same problem which exists with the Community Reinvestment language — that of placing the state banks at a disadvantage — exists here as well because “[t]hese provisions single out state-chartered banks among commercial banks and other depository institutions in Ohio and subject only state-chartered banks to discrimination tests based on only one facet of commercial bank lending.” The problem is somewhat more severe in this case in that there is no anti-redlining language in any of the federal branching laws. Thus the federal banks do not have to deal with anti-redlining, operating under the Community Reinvestment Act, instead.

The primary purpose clause in the new state branching act poses other problems. It is not realistic to require that the primary purpose of the proposed branch be to meet the credit needs of the area in which the branch is to be located. It is necessary to:

recognize that it is normal within the branching system of virtually every commercial bank (whether in Ohio or elsewhere) for some branches of the bank to produce more deposits than loans and

109 Testimony of Dr. Douglas V. Austin, supra note 159 at 11, 12.
110 Id.
111 Id. at 12. See also testimony of R. Hal Nichols, supra note 159, at 2.
112 Testimony of Roman J. Gerber, supra note 159, at 2.
113 See text accompanying note 77 supra.
114 Testimony of Roman J. Gerber, supra note 159, at 4.
for other branches to produce more loans than deposits. Inevitably, and
to the very good fortune of the various areas served by the bank, the
excess deposits generated by some branches are available to meet the
excess loans generated by other branches of the same bank. For this
reason, any legislative provision which requires that a branch has as
its primary purpose the extension of credit in the area to be served by
the bank, either reflects total ignorance of banking or economic realities
or constitutes an irresponsible tactic to obstruct the passage of liberal-
ized branching. Moreover, so long as a branch is defined to include
automatic teller machines and other electronic devices which accept de-
posits, receive loan payments, and advance funds from deposit accounts
as well as from pre-arranged lines of credit so that such devices are sub-
ject to the location and other restrictions of branching law, to require
that the primary purpose of a branch be to extend credit within its
community would be nothing less than total absurdity.\footnote{175}

The question then arises as to whether national banks will be at a dis-
tinct advantage over state banks in that, due to their seemingly less stringent
branching laws, they might be better able to take advantage of statewide
branching. The fact that this new state legislation affects only state-chartered
banks and not national banks, savings and loans, mortgage companies,
insurance companies, credit unions, or any other mortgage lender in Ohio
seems to suggest that the only loser is the state-chartered bank.

The data required of a state-chartered bank in complying with this
legislation places the state-chartered banks at a severe disadvantage relative
to other financial institutions, especially national banks. While obtaining
approval for a new branch office could easily require triple the time and
triple the cost for a state bank, a national bank would not suffer this extra
regulatory burden.\footnote{176} To impose such anti-redlining and primary purpose
provisions on only state-chartered banks in Ohio “would be to reduce their
effectiveness as competitors, to accelerate their conversion to national banks,
and, ultimately, to eliminate a viable state-chartered banking system in
Ohio.”\footnote{177}

Conversion of state banks to national banks as a result of the new
legislation is a very real problem. According to the Superintendent of Banks,
“There is very little question . . . that [Ohio’s] most aggressive, expansion-

\footnote{175} \emph{Id.} at 4, 5.
\footnote{176} Testimony of R. Hal Nichols, \emph{supra} note 159, at 2.
\footnote{177} Testimony of Roman J. Gerber, \emph{supra} note 159, at 5.
minded state banks will convert to national charters overnight in order to avoid compliance with S.B. 256."\textsuperscript{178}

The Office of the Comptroller of the Currency says that it is "a judgment call" as to whether the state or federal procedure is more stringent.\textsuperscript{179} The Comptroller maintains that the federal criteria for branching in Ohio will remain unchanged, despite the addition of the more restrictive language to the Ohio statute. The Comptroller's Office prefers to "wait until something happens"; in which event, the Comptroller will be sued by a state bank and lose; at which time, the national banks in Ohio will adopt a standard more in line with the state law, or the Comptroller will be sued and win; at which time, the state standard will be ruled unreasonable.\textsuperscript{180} The reason for this "wait and see" policy is that "it is not clear as to whether the burden is on the state or the Comptroller to change." However, the Comptroller asserts that if a problem does arise between the state and national banks, a policy statement will most likely be issued in an attempt to square the federal standard with that of the state.\textsuperscript{181}

Thus, it is clear that Senate Bill 256 has more extensive implications than its drafters expected. The idea of liberalizing the geographic restrictions is clearly in the best interest of the banking industry in Ohio. However, the procedural problems seem to pose a threat greater than that posed by restrictive branching laws. Whether this new legislation will promote the convenience and needs of the public in Ohio or endanger the banking industry itself remains to be seen.

\textbf{Benito C. R. Antognoli}

\textsuperscript{178} Testimony of R. Hal Nichols, \textit{supra} note 159, at 5. He went on to support this statement by citing to various bankers who had already testified before the committee about their concerns with the procedural requirements and their intentions to convert to national bank charters.

\textsuperscript{179} Interview with David Hack, Assistant Corporate Director, Office of the Comptroller of

\textsuperscript{180} \textit{Id.}

\textsuperscript{181} \textit{Id.}

the Currency, Cleveland, Ohio, (September 30, 1978).